Supreme Court, U. S.
FILED
SEP 22 1978
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IN THE

Supreme Court of the United States

OCTOBER TERM, 1978

No. 78-493

EDWARD S. REDINGTON, as Trustee for the liquidation of the business of Weis Securities, Inc.,

Petitioner,

—against—

TOUCHE ROSS & Co., and SECURITIES INVESTOR PROTECTION CORPORATION,

Respondents.

CROSS-PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

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IN THE

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Petitioner,

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TOUCHE ROSS & Co., and SECURITIES INVESTOR PROTECTION CORPORATION,

Respondents.

CROSS-PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

Petitioner Edward S. Redington (the "Trustee") hereby requests that a writ of certiorari issue to review the decision of the Court of Appeals for the Second Circuit, entered on April 21, 1978.

The Trustee was appointed by order of the United States District Court for the Southern District of New York to liquidate the business of Weis Securities, Inc., ("Weis") pursuant to the Securities Investor Protection Act of 1970, 15 U.S.C. §§ 78aaa *et seq.* ("SIPA" or the "1970 Act").[1] Prior to its liquidation Weis had been a broker-dealer in securities and a member of the New York Stock Exchange, Inc. ("the Exchange").

1. After this action was commenced, the Securities Investor Protection Act was amended in certain respects in 1978. Pub. L. No. 95-283, 92 Stat. 249 (1978). Where reference is made to the act as it existed before the amendments it will be called the "1970 Act."

A petition for certiorari, dated August 23, 1978, has previously been filed in this case by Touche Ross & Co. ("Touche Ross"), the defendant-appellee below. The Trustee is submitting a brief in opposition to Touche Ross' petition contemporaneously herewith.

Opinions Below

The opinion of the Court of Appeals (1a-35a)[2] is unofficially reported at [Current] Fed. Sec. L. Rep. (CCH) ¶ 96,404. The opinion of the United States District Court for the Southern District of New York (40a-58a) is reported at 428 F. Supp. 483.

Jurisdiction

The judgment of the Court of Appeals was entered on April 21, 1978 (36a-37a). On July 7, 1978, the Court of Appeals denied Touche Ross' timely petition for rehearing (38a-39a). This Court's jurisdiction is invoked under 28 U.S.C. § 1254(1).

Questions Presented

1. Whether, by filing regular and priority proofs of claim in a bankruptcy or SIPA liquidation proceeding, a claimant subjects himself to the summary jurisdiction of the district court as a Court of Bankruptcy (a) as to any adverse claim by a Trustee that is reasonably related to the creditor's claim or involves overlapping proof, or (b) as to any adverse claim by a Trustee that would be considered "mutual" under Section 68a of the Bankruptcy Act, or (c) only as to adverse claims by a Trustee that arise from the same transaction or occurrence as the creditor's claim?

2. Whether Congress conferred on a district court supervising a SIPA liquidation under the 1970 Act the full

2. Numerals followed by the letter "a" refer to pages of the Appendix attached to Touche Ross' petition.

plenary jurisdiction of a Chapter X or federal equity receivership court, rather than the more limited plenary jurisdiction of a district court supervising a bankruptcy under Chapters I-VII of the Bankruptcy Act?

Statutes And Rules Involved

Sections 2a(7), 23, 102 and 115 of the Bankruptcy Act, 11 U.S.C. §§ 11a(7), 46, 502 and 515, and sections 5(b)(2), 6(b)(1) and 6(c)(1) of the 1970 Act, 15 U.S.C. §§ 78eee(b)(2), fff(b)(1) and fff(c)(1) as in force when this action was commenced are set forth in relevant part in the Appendix hereto.

Statement Of The Case

The facts underlying this action are more fully set forth in the Trustee's brief in opposition to Touche Ross' petition and in the brief in opposition submitted by the Trustee's co-respondent and co-plaintiff below, the Securities Investor Protection Corporation ("SIPC"). Only certain salient facts need be highlighted herein.

In 1972 Touche Ross, a firm of certified public accountants, audited Weis and certified the adequacy of Weis' financial statements "as at May 26, 1972" under Section 17 of the Securities Exchange Act of 1934, 15 U.S.C. §§ 78a *et seq.* (the "Exchange Act"), and the rules and regulations thereunder; the audit failed to detect false and fraudulent entries in Weis' books and records, substantial overstatements of Weis' profitability and net worth and serious misstatements of its net capital ratio. The audit is alleged to have been at least negligent, if not grossly negligent and reckless, and to have been the proximate cause of a SIPA

liquidation in which the Trustee has not been able to make all of Weis' customers and creditors whole.

In the complaint (reproduced in the Appendix to SIPC's brief in opposition to Touche Ross' petition), the Trustee asserted six separate claims for relief against Touche Ross.[3] One of these claims was predicated on Section 17 of the Exchange Act and is the subject of Touche Ross' petition.

The Trustee's other five claims for relief involve causes of action under state and common law principles of negligence, breach of contract and breach of warranty. The Trustee asserted these claims in his derivative capacity as representative of Weis and as bailee of the property entrusted to Weis by its customers. Jurisdiction over these non-federal claims was based on principles of pendent jurisdiction and on the jurisdiction of the District Court as a Court of Bankruptcy under the 1970 Act and the provisions of the Bankruptcy Act incorporated into that Act.

Court of Bankruptcy Jurisdiction and Touche Ross' Consent

The Trustee had two grounds for invoking the jurisdiction of the District Court as a Court of Bankruptcy. First, the 1970 Act specifically gave the District Court the "powers" of a Chapter X court and a federal equity receivership court as well as a court supervising an ordinary bankruptcy. A Chapter X or federal equity receivership court would of course have *plenary* jurisdiction over any action commenced by the Trustee in his home court.

Second, Touche Ross had consented to the *summary* jurisdiction of the District Court as a Court of Bankruptcy by submitting two proofs of claim in the Weis liquidation. One

3. Eight claims are also asserted by SIPC. SIPC, however, asserted different jurisdictional bases for its non-federal claims.

claim sought $67,972 for commencing work on Weis' 1973 audit as well as a smaller amount ($7,471) for services performed by Touche Ross at Weis' London and Paris offices. The other claim sought $11,664 for services allegedly rendered in connection with the investigation of Weis' books and records conducted in late April and May of 1973 by the Securities and Exchange Commission and the New York Stock Exchange. The bulk of this claim is attributable to meetings with the SEC and the Exchange and "[s]ubstantiation and documentation of alleged fraudulent bookkeeping practices and entries." These are the very practices and entries which prevented Weis from being saved as a going concern and for which the complaint alleges that Touche Ross was responsible.

The District Court's Treatment of the Jurisdictional Issues

The District Court dismissed the complaint in its entirety. Stating that "[t]he arguments for the Trustee have been considered but cannot be accepted" (56a), the Court held that it had only the plenary jurisdiction of a court supervising a bankruptcy rather than the broader jurisdiction of a Chapter X or federal equity receivership court (56a). The Court also held that Touche Ross did not consent to the summary jurisdiction of the Court for the Trustee's claims because the claims of Touche Ross and the Trustee were not "mutual" within the meaning of Section 68 of the Bankruptcy Act. (*Id.*)

The Court's discussion of Touche Ross' claims was extremely perfunctory. The Court ignored the claim that sought recovery for substantiation of the fraud and bookkeeping irregularities underlying the 1972 audit. Instead, the Court emphasized only the small portion of one of the

claims which involved the services rendered by Touche Ross at Weis' London and Paris branch offices. The Court's analysis of the issue is contained in the following two sentences:

> "[T]he claim filed by Touche in the Weis liquidation was for accounting work in *European offices of Weis* in late 1972 and early 1973, as well as for a Stock Exchange audit as of April 27, 1973. The claim by the Trustee against Touche does not arise out of any work done for Weis by Touche and for which Touche filed a claim in the Weis liquidation. The claims are not 'mutual' therefore but are unrelated and the consent of Touche cannot be found. • • •" (Citation omitted; emphasis in original.) (56a.)

The Court of Appeals' Failure to Reach the Jurisdictional Issues

The question of the District Court's plenary and summary jurisdiction as a Court of Bankruptcy was briefed extensively by both the Trustee and Touche Ross in the Court of Appeals.[4] However, the Court of Appeals, in sustaining federal jurisdiction over the Trustee's Section 17 claim, stated that "[b]ecause of the view we take of the case, we need express no opinion as to the scope of bankruptcy jurisdiction in SIPA-receivership cases . . . " (3a n. 3.) The court also did not decide the question of pendent jurisdiction but remanded the case to the District Court for further proceedings including a determination of that issue. (15a.)

The Court of Appeals' refusal to decide the extent of the District Court's jurisdiction as a Court of Bankruptcy has

4. The Trustee devoted approximately fifteen pages of his main brief and ten pages of his reply brief to these issues; Touche Ross, approximately thirty-two pages of its brief in opposition.

left this action in a peculiar posture. As matters now stand, if the District Court on remand were to refuse to exercise pendent jurisdiction (or if this Court were to accept certiorari and reverse on the Section 17 question) the Trustee could find that he is out of federal court on his non-Section 17 claims for relief, without ever having had a resolution of the question of jurisdiction over these claims. Even aside from the national importance of the jurisdictional question (which is discussed more fully below at pp. 7-12), this Court should grant certiorari at least for the purpose of remanding for orderly consideration of the jurisdictional issues by the Court of Appeals.

Reasons for Granting the Writ

I.

The Extent Of A Claimant's Consent To The Jurisdiction Of A Court Of Bankruptcy Under Section 23 Of The Bankruptcy Act Is An Important And Recurring Question Of Law That Has Not Been, But Should Be, Decided By This Court.

Section 23b of the Bankruptcy Act (11 U.S.C. § 46b) expressly provides for the granting of summary jurisdiction by consent as follows:

> "Suits by the receiver and the trustee shall be brought or prosecuted only in the courts where the bankrupt might have brought or prosecuted them if proceedings under this Act had not been instituted, *unless by consent of the defendant* • • •" (Emphasis added.)[5]

5. Section 23b is a limitation on the broad jurisdiction conferred on district courts as courts of bankruptcy by Congress in Section 2a(7) of the Bankruptcy Act. There is no dispute that a district court supervising a SIPA liquidation has at least the jurisdiction conferred by Section 23b. As explained in Point II below, Touche Ross does dispute whether the 1970 Act contained a broader grant of jurisdiction to the district court.

A claimant who files a proof of claim in a bankruptcy or SIPA liquidation consents to the jurisdiction of a Court of Bankruptcy with respect to issues involved in determining that claim and certain counterclaims. *See Katchen* v. *Landy,* 382 U.S. 323, 326 n.1 (1966). Section 23b does not, however, provide any guidance on the issue of what adverse claims a claimant consents to have adjudicated by a Court of Bankruptcy by filing a proof of claim. This Court has never ruled on the issue apart from the context of an adverse claim by a trustee to recover a preferential transfer.

Resolution of the question of what other adverse claims a creditor consents to have adjudicated by a Court of Bankruptcy when he files a proof of claim is important to the administration of both the Bankruptcy Act and SIPA and would have a significant impact on the conduct of bankruptcy proceedings throughout the federal courts. As the House Judiciary Committee has noted in reporting on the need for revision of the bankruptcy laws:

> "Under the current bankruptcy law, the jurisdiction of the bankruptcy [court] is limited by the concept of possession, either actual or constructive, or consent, either express or implied. An enormous case law has developed around this provision. Volumes have been written on what constitutes adequate possession to give the bankruptcy court jurisdiction, and on what constitutes adequate consent. * * * In an area of law in which time is of the essence, the delay attendant upon litigation over jurisdiction is needless and expensive." (Footnotes omitted.)

Report of the House Comm. on the Judiciary on Bankruptcy Law Revision, H.R. Rep. No. 95-595, 95th Cong. 1st Sess. 43 (1977). *See also* Report of the Commission on the Bankruptcy Laws of the United States, H.R. Doc. No. 93-137, Part 1, 89-90 (1973).

Although issues concerning the scope of the jurisdiction conferred on the bankruptcy courts by "consent of the defendant" under Section 23b arise frequently in bankruptcy and liquidation proceedings, no uniform standard is followed by the lower federal courts for determining this issue; instead, a number of different approaches are used which make it difficult, if not impossible, for litigants to predict the extent to which a Court of Bankruptcy may choose to exercise its summary jurisdiction. A decision by this court resolving this confusion would not only permit courts of bankruptcy to decide uniformly issues pertaining to their own summary jurisdiction but, perhaps even more importantly, it would clarify for claimants and litigants in bankruptcy proceedings throughout the country their rights and liabilities in subjecting themselves to the jurisdiction of a Court of Bankruptcy.

More than a decade ago in *Katchen* v. *Landy,* 382 U.S. 323 (1966), this court accepted certiorari to decide a related question because of its importance to the administration of the Bankruptcy Act. Id. at 326. The Court there held that where a creditor submits a claim in bankruptcy summary jurisdiction exists in the Court of Bankruptcy to order the return of a voidable preference because the determination of whether a claimant has received a voidable preference is a prerequisite to determining the size and allowability of his claim under Section 57g of the Bankruptcy Act (11 U.S.C. § 93g). The Court reasoned that, the determination that there had been a preference would be *res judicata* in any later plenary suit brought by the Trustee to recover the preference, and therefore concluded that "it can hardly be doubted that there is also summary jurisdiction to order the return of the preference." 382 U.S. at 334. *Katchen* did not decide whether the same rule applied to other types of claims by a Trustee because the petition for certiorari in that case had been limited to the preferential transfer question. *Id.* at 326.

The rationale applied by this Court in *Katchen* logically applies to any "mutual debts" since, under Section 68a of the Bankruptcy Act (11 U.S.C. § 108a) such mutual debts must be set off and "the balance only . . . allowed or paid."[6] As with preferences, such claims seemingly must be determined in order to determine the size and allowability of the creditor's claim. Thus, once a claimant files its proof of claim, summary jurisdiction should exist to adjudicate the merits of any mutual claim, even a wholly unrelated claim, as a set-off which would diminish or defeat the creditor's claims. See *Conway* v. *Union Bank of Switzerland,* 204 F.2d 603, 607 (2d Cir. 1953); *United States* v. *Roth,* 164 F.2d 575, 578 (2d Cir. 1948); 4 W. Collier, *Bankruptcy* § 68.20[4] at 946 (14th ed. 1978). See 3 *Moore's Federal Practice* ¶ 13.19[1] at 482-83 (1978). And, as in *Katchen,* once the merits of the adverse claim have been adjudicated between the parties in a Court of Bankruptcy, that adjudication should be *res judicata* in any later action brought to recover the balance by which a Trustee's counterclaim exceeds the creditor's original claim. *Conway* v. *Union Bank of Switzerland, supra,* 204 F.2d at 607; *Schwartz* v. *Levine & Malin, Inc.,* 111 F.2d 81 (2d Cir. 1940). Accordingly, the principle of *Katchen* v. *Landy* should logically extend not only to preferences but to any mutual claim capable of being set-off under Section 68.

However, the lower federal courts have not applied the same rational as *Katchen.* Instead, they have applied a

6. Section 68 provides in pertinent part as follows:

"Section 68. Set-Offs and Counterclaims.

a. In all cases of mutual debts or mutual credits between the estate of a bankrupt and a creditor the account shall be stated and one debt shall be set off against the other, and the balance only shall be allowed or paid."

The District Court apparently believed that mutuality under Section 68 should be the controlling standard but erred in its consideration of that standard. (56a.) Claims are "mutual" within the meaning of Section 68 if they are "in the same right and between the same parties, standing in the same capacity." 4 W. Collier, *Bankruptcy* ¶ 68.04 [2-1] at 867 (14th ed. 1978); *United States* v. *Roth,* 164 F.2d 575, 578 (2d Cir. 1948).

number of different standards which makes it difficult, if not impossible, to predict the extent to which a particular Court of Bankruptcy may choose to exercise its summary jurisdiction.

In the Second Circuit, for example, a party is deemed to consent to the court's jurisdiction and voluntarily submits to the federal court not only in regard to securing his own relief, but to any claim which the Trustee might reasonably raise against him in the same proceeding pursuant to his duty to collect the estate. *Nortex Trading Corp.* v. *Newfield,* 311 F.2d 163, 164 (2d Cir. 1962); *Chase National Bank* v. *Lyford,* 147 F.2d 273, 277 (2d Cir. 1945); *Liman* v. *United Kingdom Mutual Steamship Assurance Association,* 297 F. Supp. 577, 579-81 (S.D.N.Y.), *appeal dismissed,* 418 F.2d 9 (2d Cir. 1969); *In re Ira Haupt & Co.,* 289 F. Supp. 966, 970-71 (S.D.N.Y. 1968); *see Beldock* v. *Faberge Inc.,* 4 Bankr. Ct. Dec. 432 (1978) (decision of Bankruptcy Judge Galgay). All that appears to be required is a logical relationship between the respective claims, or overlapping proof. *E.g., In re Farrel Publishing Corp.,* 130 F. Supp. 449, 452 (S.D.N.Y. 1955) ("In effect the [Bankruptcy] Act declares a statutory policy to settle all related claims."); *Liman* v. *United Kingdom Mutual Steamship Assurance Association, supra; In re Ira Haupt & Co., supra. See generally, Moore* v. *New York Cotton Exchange,* 270 U.S. 593, 609-10 (1926); *United States* v. *Heyward-Robinson Co.,* 430 F.2d 1077 (2d Cir. 1970), *cert. denied,* 400 U.S. 1021 (1972); *United Artists Corp.* v. *Masterpiece Productions, Inc.,* 221 F.2d 213, 216 (2d Cir. 1955).

Other courts, though also recognizing the principle of consent to the jurisdiction of a Court of Bankruptcy, appear to apply a somewhat stricter standard. These cases suggest that the consent to jurisdiction to be implied from the invocation of the jurisdiction of a Court of Bankruptcy is limited to "closely related" claims or claims in the nature of "compulsory counterclaims". *Peters* v. *Lines,* 275 F.2d 919, 925 (9th Cir. 1960); *Nissho American Corp.* v. *Humphreys,* 445 F.2d 1096, 1098-99 (5th Cir. 1971), *cert. denied,* 404 U.S. 991 (1971); *Masterson* v. *Valley National Bank,* 424 F.2d 296, 298-99 (3d Cir. 1970); *Associate Funding, Inc.* v. *Phipps,* 464 F.2d 1136, 1138-39 (9th Cir.), *cert. denied,* 409 U.S. 1064 (1972); *Dwyer* v. *Franklin,* 227 F.2d 152, 156 (7th Cir. 1955), *cert. denied,* 350 U.S. 995 (1956); *Liberty Mutual Insurance Co.* v. *Mann,* 73 F.R.D. 295, 296 (E.D. Mo. 1976); *In re Beasley-Gilbert's, Inc.,* 285 F. Supp. 359, 361 (S.D. Ohio 1968).

Here, the Trustee's claims arose out of Touche Ross' ongoing role as Weis' accountants preceding the commencement of the Weis liquidation; the evidence relevant to Touche Ross' claims will overlap the evidence necessary to support the Trustee's claims; and some of Touche Ross' claims involve work done with respect to the very false entries which the Trustee alleges Touche Ross failed to detect in its 1972 audit. Accordingly, both mere mutuality and logical relationship exist between the Trustee's and Touche Ross' claims, although they may not be closely related enough to satisfy a strict compulsory counterclaim standard. At a time when the need to clarify the jurisdiction of Courts of Bankruptcy is widely recognized, this case presents a uniquely appropriate factual opportunity for this Court to resolve the question of what standard should be applied under Section 23b.

II.

This Court Should Exercise Its Powers Of Supervision To Determine The Extent Of The Jurisdiction Conferred On District Courts Under The 1970 Act, Or Remand To The Court Of Appeals For Consideration Of That Issue.

Under the 1970 Act, jurisdiction of SIPA courts is determined by reference to Sections 5 and 6 of that Act (15 U.S.C. §§ 78eee and 78fff) and Sections 2a(7), 102 and 115 of the Bankruptcy Act (11 U.S.C. §§ 11(a)(7), 502 and 515), as made applicable by the 1970 Act. These provisions confer on the district courts supervising SIPA liquidations the "powers" of a court supervising a Chapter X proceeding (the 1970 Act §§ 5(b)(2), 6(b)(1)) as well as the power of a district court supervising an equity receivership under Section 115 of the Bankruptcy Act.

In Section 5(b)(2) of the 1970 Act Congress expressly provided that a court in which a SIPA proceeding is initiated shall have the *"powers . . .* of a court of bankruptcy *and* of a court in a proceeding under Chapter X of the Bankruptcy Act." (Emphasis added.)[7] Under the decisions of this Court, this grant of "power" to a federal court is a jurisdictional grant. *United Mine Workers* v. *Gibbs,* 383 U.S. 715, 725 (1966); *Kendall* v. *Stokes,* 37 U.S. (12 Pet) 524, 622-23 (1838); *Rudick* v. *Laird,* 412 F.2d 16, 20 (2d Cir.), *cert. denied,* 396 U.S. 918 (1969). In *Williams* v. *Austrian,* 331 U.S. 642, 659-60 n.45 (1947), this Court noted that the "powers" provision in Section 115 of the Bankruptcy Act "has been interpreted as jurisdictional" by the

7. In Section 6(b)(1) of the 1970 Act Congress augmented and reinforced the grant of "power" to the District Courts contained in Section 5(b)(2) by providing a SIPA Trustee with all the powers of both a bankruptcy and a Chapter X Trustee. *See SEC* v. *Albert & Maguire Securities Co.,* 560 F.2d 569, 574 (3d Cir. 1977); 3 W. Collier, Bankruptcy ¶ 60.85[2] at 1247 (14 ed. 1977).

federal courts. Article III of the Constitution itself uses the word "power" in this jurisdictional sense.

By providing the SIPA court with the "power" of a Chapter X court, Congress conferred on SIPA courts the full range of "power" conferred on district courts under the bankruptcy clause in Section 2b of the Bankruptcy Act (11 U.S.C. § 11b). This grant includes the plenary jurisdictional "power" conferred by Section 2a(7) and exercised in actions brought by Chapter X trustees.[8] *See Williams* v. *Austrian*, 331 U.S. 642, 646 (1947). This grant of jurisdiction to SIPA courts is more than ample to support non-federal claims such as the Trustee's in this case.

The District Court, however, rejected the application of these provisions to the issue of jurisdiction and instead focused improperly on Section 6(c)(1) of the 1970 Act. Relying on that section—which deals with the conduct of liquidation proceedings, not the jurisdiction of the district court—the Court erroneously concluded that its jurisdiction was limited by Section 23 of the Bankruptcy Act to that of a court supervising bankruptcy proceedings under Chapters I-VII of the Bankruptcy Act. (55a-56a.)[9]

8. The grant also includes the jurisdictional Section 115 (11 U.S.C. § 515) which gives the federal court of the trustee's appointment all the ancillary jurisdiction of the "home court" in federal equity receiverships. That jurisdiction entitles the Court which appointed such a receiver to adjudicate any action instituted by its receiver (here the Trustee) regardless of the existence of independent jurisdictional grounds. *See Riehle* v. *Margolies*, 279 U.S. 218, 223 (1929).

9. Section 23 is not referred to anywhere in the 1970 Act, but Section 6(c)(1) does refer to sections referred to in Section 102 of the Bankruptcy Act. Section 23 is one such section. Except in cases of consent, and in actions involving preferential or fraudulent transfers, Section 23 limits the district court's jurisdiction over an action between a trustee and an adverse party to that which would have existed in an action between the bankrupt and the adverse party before the bankruptcy. Section 6(c)(1) states, however, that such provisions of the Bankruptcy Act as it may incorporate apply to the conduct of liquidation proceedings only to the extent that they are consistent with the other provisions of the 1970 Act. Were Section 6(c)(1) interpreted as jurisdictional and its indirect reference to Section 23 interpreted to determine the jurisdiction of SIPA courts, the section would be rendered inconsistent with Section 5(b)(2).

Although the recent amendments to SIPA have altered some of the language of the 1970 Act, the extent of a SIPA court's jurisdiction remains an important, unresolved issue. Moreover, as explained at pages 6-7 *supra*, review or remand on the plenary jurisdictional question as well as the consent question is necessary to cure the Second Circuit's error in failing to reach the jurisdictional issues.

Conclusion

For the foregoing reasons, the Trustee's cross-petition for a writ of certiorari should in all respects be granted.

Dated: September 22, 1978

Respectfully submitted,

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APPENDIX

Securities Investor Protection Act of 1970, as in effect prior to the Securities Investor Protection Act Amendments of 1978, Pub. L. No. 95-283, 92 Stat. 249 (1978).

Sec. 5(b)(2) (15 U.S.C. § 78eee(b)(2)).

> "(2) EXCLUSIVE JURISDICTION OVER DEBTOR.—Upon the filing of an application pursuant to subsection (a)(2), the court to which application is made shall have exclusive jurisdiction of the debtor involved and its property wherever located with the powers, to the extent consistent with the purposes of this Act, of a court of bankruptcy and of a court in a proceeding under chapter X of the Bankruptcy Act."

Sec. 6(b)(1) (15 U.S.C. § 78fff(b)(1)).

> (1) TRUSTEE POWERS.—A trustee appointed under section 5(b)(3) (hereinafter referred to as "trustee") shall be vested with the same powers and title with respect to the debtor and the property of the debtor, and the same rights to avoid preferences, as a trustee in bankruptcy and a trustee under chapter X of the Bankruptcy Act have with respect to a bankrupt and a chapter X debtor."

Sec. 6(c)(1) (15 U.S.C. § 78fff(c)(1)).

> "(1) GENERAL PROVISIONS APPLICABLE.—Except as inconsistent with the provisions of this Act and except that in no event shall a plan of reorganization be formulated, a liquidation proceeding shall be conducted in accordance with, and as though it were being conducted under, the provision of chapter X and such of the provisions (other than section 60e) of chapters I to VII, inclusive, of the Bankruptcy Act as section 102 of chapter X would make applicable if an order of the court had been entered directing that bankruptcy be proceeded with pursuant to the provisions of such chapters I to VII, inclusive * * *."

Bankruptcy Act

Sec. 2a(7) (11 U.S.C. § 11(a)(7)).

"a. The courts of the United States hereinbefore defined as courts of bankruptcy are hereby created courts of bankruptcy and are hereby invested, within their respective territorial limits as now established or as they may be hereafter changed, with such jurisdiction at law and in equity as will enable them to exercise original jurisdiction in proceedings under this Act, in vacation, in chambers, and during their respective terms, as they are now or may be hereafter held, to—

* * * (7) Cause the estates of bankrupts to be collected, reduced to money, and distributed, and determine controversies in relation thereto, except as herein otherwise provided * * *."

Sec. 23 (11 U.S.C. § 46).

"a. The United States district courts shall have jurisdiction of all controversies at law and in equity, as distinguished from proceedings under this Act, between receivers and trustees as such and adverse claimants, concerning the property acquired or claimed by the receivers or trustees, in the same manner and to the same extent as though such proceedings had not been instituted and such controversies had been between the bankrupts and such adverse claimants.

b. Suits by the receiver and the trustee shall be brought or prosecuted only in the courts where the bankrupt might have brought or prosecuted them if proceedings under this Act had not been instituted, unless by consent of the defendant, except as provided in sections 60, 67, and 70 of this Act."

Sec. 68a (11 U.S.C. § 108a).

§ *68. Sets-Offs and Counterclaims.* **a. In all cases** of mutual debts or mutual credits between the estate of a bankrupt and a creditor the account shall be stated and one debt shall be set off against the other, and the balance only shall be allowed or paid.

Sec. 102 (11 U.S.C. § 502).

"The provisions of chapters I to VII, inclusive, of this Act shall, insofar as they are not inconsistent or in conflict with the provisions of this chapter, apply in proceedings under this chapter: *Provided, however,* That section 23, subdivisions h and n of section 57, section 64, and subdivision f of section 70, shall not apply in such proceedings unless an order shall be entered directing that bankruptcy be proceeded with pursuant to the provisions of chapters I to VII, inclusive."

Sec. 115 (11 U.S.C. § 515).

"Upon the approval of a petition, the court shall have and may, in addition to the jurisdiction, powers, and duties hereinabove and elsewhere in this chapter conferred and imposed upon it, exercise all the powers, not inconsistent with the provisions of this chapter, which a court of the United States would have if it had appointed a receiver in equity of the property of the debtor on the ground of insolvency or inability to meet its debts as they mature."

Supreme Court, U. S.
FILED
OCT 23 1978
MICHAEL RODAK, JR., CLERK

IN THE

Supreme Court of the United States

OCTOBER TERM, 1978

No. 78-493

EDWARD S. REDINGTON, as Trustee for the liquidation of the business of Weis Securities, Inc.,

Petitioner,

–against–

TOUCHE ROSS & CO., and SECURITIES INVESTOR PROTECTION CORPORATION,

Respondents.

BRIEF OF RESPONDENT TOUCHE ROSS & CO. IN OPPOSITION TO THE CROSS-PETITION FOR A WRIT OF CERTIORARI

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IN THE

Supreme Court of the United States

OCTOBER TERM, 1978

No. 78-493

EDWARD S. REDINGTON, as Trustee for the liquidation of the business of Weis Securities, Inc.,

Petitioner,

–against–

TOUCHE ROSS & CO., and SECURITIES INVESTOR PROTECTION CORPORATION,

Respondents.

BRIEF OF RESPONDENT TOUCHE ROSS & CO. IN OPPOSITION TO THE CROSS-PETITION FOR A WRIT OF CERTIORARI

Respondent Touche Ross & Co. ("Touche Ross"), which is also petitioner in No. 78-309 and respondent in No. 78-526, submits this brief in opposition to the cross-petition of Edward S. Redington (the "Trustee"), as Trustee for the liquidation of the business of Weis Securities, Inc. ("Weis"), for a writ of certiorari to review the decision of the United States Court of Appeals for the Second Circuit entered herein on April 21, 1978.[1]

[1]The decisions below are reproduced in the Appendix to Touche Ross' Petition in No. 78-309. Numerals followed by the letter "a" are page references to that Appendix.

COUNTER-STATEMENT OF THE QUESTIONS PRESENTED

1. Was the District Court correct in its holding (as to which the Court of Appeals stated that it expressed no opinion) that, by filing proofs of claim in the proceeding to liquidate the business of a defunct securities brokerage firm under the Securities Investor Protection Act of 1970, a creditor did not "consent" to the jurisdiction of the District Court in a separate *plenary* action subsequently commenced by the trustee on unrelated state common law claims against the creditor?

2. Was the District Court correct in its holding (as to which the Court of Appeals stated that it expressed no opinion) that, unlike a Chapter X reorganization court or a federal equity receivership court, its plenary jurisdiction was limited by Section 23 of the Bankruptcy Act, which was incorporated into the Securities Investor Protection Act of 1970 by Section 6(c)(1) thereof?

COUNTER-STATEMENT OF THE CASE

The Trustee, who was appointed and is acting pursuant to the Securities Investor Protection Act of 1970 ("SIPA"), is liquidating the business of Weis, a defunct brokerage firm which collapsed in May 1973. The Trustee and respondent Securities Investor Protection Corporation ("SIPC") commenced this plenary action against Touche Ross in April 1976 in the United States District Court for the Southern District of New York, asserting both federal claims (under Section 17(a) of the Securities Exchange Act of 1934 (the "1934 Act")) and common law claims seeking damages from Touche Ross by reason of its allegedly improper audit of financial reports (the "1972 Weis financial reports") of Weis for periods ending May 26, 1972. The commencement of this plenary federal action occurred almost a year after the Trustee and SIPC had commenced a still-pending, almost identical plenary action (the "State Court Action") against Touche Ross in the New York state courts.[2]

Touche Ross' Petition in No. 78-309 seeks to have this Court review the decision of the Court of Appeals majority reversing the District Court and holding that the Trustee and SIPC are entitled to assert federal claims under Section 17(a) of the 1934 Act. The Trustee's cross-petition seeks to have this Court review the decision of *the District Court* that the Bankruptcy Act (provisions of which are incorporated into SIPA) does not grant subject matter jurisdiction over the Trustee's common law claims—a decision which the Court of Appeals left undisturbed and as to which it "express[ed] no opinion" (3a[n.3]).

The pertinent facts, which also are set forth in relevant part in Touche Ross' Petition in No. 78-309, may be briefly summarized as follows:

A. The Trustee's Common Law Claims

In the complaint herein (just as in the complaint in the State Court Action), the Trustee seeks relief with respect to Touche Ross' alleged conduct of its mid-1972 audit of the 1972 Weis financial reports. According to the complaint,[3] certain officers of Weis had misstated the

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[2]The State Court Action was commenced in July 1975. The only material difference in the two actions is the addition in the complaint in this action of the few allegations deemed by the Trustee and SIPC to be necessary to assert claims under Section 17(a) of the 1934 Act. As the Court of Appeals majority put it, "[t]he common allegations of the plaintiffs in the state court complaint were the same as those in the instant case, except that three paragraphs dealing with claims under section 17 of the [19]34 Act were omitted. Five of the Trustee's six present 'causes of action' appear in identical form in the state action, as do four of SIPC's eight present claims. The additional claims in this action are the federal securities law claims" (5a).

[3]The complaint is reproduced in the appendix to SIPC's brief in opposition to Touche Ross' Petition in No. 78-309.

financial condition and results of operations of Weis in the 1972 Weis financial reports, and had made it appear therein that Weis had pre-tax earnings for the fiscal year of $1,700,000, whereas Weis actually had suffered losses in excess of $1,500,000. Touche Ross allegedly performed its audit of the 1972 Weis financial reports in a "negligent, reckless, careless, unskilled and grossly negligent manner", and therefore not only failed to discover the misstatements but also improperly certified that the 1972 Weis financial reports fairly and accurately presented the financial condition of Weis in accordance with generally accepted accounting principles. It is alleged that if Touche Ross had discovered the misstatements in the 1972 Weis financial reports, Weis' declining financial position and the waste of its assets would have been revealed earlier, remedial action such as a change in the Weis management or merger with another firm could have been taken, the forced liquidation of Weis could have been averted or its adverse consequences reduced, and the losses here sued for would not have occurred.

On the basis of the foregoing, the Trustee asserts (in addition to his federal claim under Section 17(a)) common law claims for accountants' negligence and malpractice, breach of contract and breach of warranty, and seeks to recover from Touche Ross damages of $51,000,000.

B. The Trustee's Jurisdictional Contentions

The Trustee's jurisdictional allegations are set forth in paragraph 2 of the complaint. After alleging that Section 27 of the 1934 Act provides jurisdiction for his federal Section 17(a) claim, he alleges as one basis for subject matter jurisdiction over his common law claims the "principles of pendent jurisdiction". However, recognizing that there would be no proper basis for the exercise of pendent jurisdiction if it were held that he may not assert a federal claim under Section 17(a), and

also recognizing that the exercise of pendent jurisdiction would be discretionary with the District Court even if his Section 17(a) claim were upheld (particularly in light of the pendency of the State Court Action asserting the identical common law claims), the Trustee also alleges that specified sections of the Bankruptcy Act provide an additional jurisdictional basis for his common law claims. Specifically, the Trustee alleges that jurisdiction is provided by "Sections 2a(7), 102 and 115 of the Bankruptcy Act (11 U.S.C. Sections 11a(7), 502 and 515)", together with "Section 6" of SIPA, which provides for reference to provisions of the Bankruptcy Act.

In seeking in the District Court to support his contention of Bankruptcy Act jurisdiction over his common law claims, the Trustee also asserted that such jurisdiction exists in this *plenary* action because of Touche Ross' purported "consent" to the bankruptcy court's *summary* jurisdiction by filing claims in the Weis liquidation proceeding for services rendered by Touche Ross to Weis in late 1972 and 1973, well after the completion of the mid-1972 audit work on the 1972 Weis financial reports.[4] However, the complaint significantly does not assert any claim relating to (or even mention) the later services, and does not allege "consent" or Section 23 of the Bankruptcy Act (which authorizes certain consent jurisdiction) as a jurisdictional basis.

---

[4]The Trustee's cross-petition (pp. 4-5) describes Touche Ross' "two proofs of claim in the Weis liquidation" as follows: "One claim sought $67,972 for commencing work on Weis' 1973 audit as well as a smaller amount ($7,471) for services performed by Touche Ross at Weis' London and Paris offices. The other claim sought $11,664 for services allegedly rendered in connection with the investigation of Weis' books and records conducted in late April and May of 1973 by the Securities and Exchange Commission and the New York Stock Exchange. The bulk of this claim is attributable to meetings with the SEC and the Exchange and '[s]ubstantiation and documentation of alleged fraudulent bookkeeping practices and entries.' "

C. The District Court's Dismissal Of This Action, And Its Rejection Of The Trustee's Contention Of Bankruptcy Act Jurisdiction

The District Court granted Touche Ross' motion to dismiss this action (40a-58a), and in so doing expressly rejected the Trustee's contention that it had subject matter jurisdiction over his common law claims.[5] The District Court first dismissed the Trustee's federal Section 17(a) claim for failure to state a claim upon which relief can be granted (47a-55a), and held that by reason of such dismissal pendent jurisdiction of the Trustee's common law claims was lacking (55a). The District Court then held that the Bankruptcy Act did not provide subject matter jurisdiction for the Trustee's common law claims (55a-57a).

With respect to the Trustee's contention of Bankruptcy Act jurisdiction, the District Court held that "[t]he situation at bar . . . is controlled by [Section 23 of the Bankruptcy Act] 11 U.S.C. § 46 which provides that a trustee in bankruptcy may sue only in the courts where the bankrupt might have sued", and that subject matter jurisdiction of the Trustee's common law claims is lacking because "[d]iversity jurisdiction would not exist of an action by Weis against Touche [Ross]" (55a-57a).[6] The District Court concluded that Section 23 is applicable and controlling because it is incorporated into SIPA by Section 6(c)(1) thereof (55a-56a).

[5]Touche Ross' motion sought, *inter alia*, (i) dismissal of the Trustee's federal Section 17(a) claim for failure to state a claim upon which relief can be granted, (ii) dismissal of the Trustee's common law claims for lack of subject matter jurisdiction, (iii) dismissal of certain of the Trustee's common law claims for failure to state a claim upon which relief can be granted, and (iv) alternatively, a stay of this action pending determination of the State Court Action. It was unnecessary for the District Court to reach, and it did not consider, issues (iii) and (iv).

[6]The Trustee has never challenged the showing to the District Court, or the District Court's finding, that both Weis and Touche Ross are citizens of New York for purposes of determining whether diversity jurisdiction exists.

The District Court "considered" and rejected the Trustee's argument that Sections 2a(7), 102 and 115 of the Bankruptcy Act, as allegedly made applicable by Sections 5(b)(2) (another provision not set forth in the Trustee's jurisdictional allegations) and 6(b)(1) of SIPA, confer upon the District Court the broad plenary jurisdiction of a Chapter X reorganization court and a federal equity receivership court—a jurisdiction which was claimed by the Trustee to extend to *any* action commenced by him (56a).

The District Court also considered and rejected the Trustee's argument, made for the first time after Touche Ross had demonstrated on its motion to dismiss that Section 23 did not permit the exercise of Bankruptcy Act jurisdiction, that Touche Ross had "consented" to such jurisdiction within the meaning of Section 23 by filing its two proofs of claim in the Weis liquidation proceeding. The District Court found that the Trustee's common law claims here for negligence and malpractice, breach of warranty, and breach of contract—claims based upon Touche Ross' mid-1972 audit of the 1972 Weis financial reports—were "unrelated" to the claims filed in the liquidation by Touche Ross for other services rendered to Weis in late 1972 and 1973, stating that "[t]he claim by the Trustee against Touche [Ross] does not arise out of any work done for Weis by Touche [Ross] and for which Touche [Ross] filed a claim in the Weis liquidation" and therefore "the consent of Touche [Ross] cannot be found" (56a).[7]

[7]Apparently because the Trustee characterized one of the Touche Ross claims as a "priority" or administrative claim, the District Court also found that such claim and the Trustee's common law claims against Touche Ross based upon services performed by Touche Ross almost a year before the Weis collapse were not "mutual" (56a). As noted (p. 5, n.4, *supra*), one of Touche Ross' proofs of claim referred in part to services performed in 1973 in connection with "[s]ubstantiation and documentation of alleged fraudulent bookkeeping practices and entries". Nothing in the record supports the Trustee's bald assertion that the practices and entries referred to in that claim are the same as the alleged fraudulent practices and entries which Touche Ross did not detect in mid-1972 (Cross-Petition, pp. 5, 12), and the District Court properly rejected that assertion.

D. The Decision Of The Court Of Appeals, And Its Express Refusal to Pass Upon The District Court's Holding That There Is No Bankruptcy Act Jurisdiction

The Court of Appeals majority reversed the District Court's holding with respect to the Trustee's federal Section 17(a) claim and remanded for further proceedings. However, the Court of Appeals majority expressly refused to pass upon the District Court's holding that there is no Bankruptcy Act jurisdiction, stating that "[b]ecause of the view we take of the case, we need express no opinion as to the scope of bankruptcy jurisdiction in SIPA-receivership cases" (3a[n.3]). Even though the Court of Appeals thus has not considered or ruled upon the question, the Trustee seeks by his cross-petition to have this Court review the District Court's holding that there is no Bankruptcy Act jurisdiction over his common law claims.

THE REASONS FOR DENYING THE CROSS-PETITION

I

Review By This Court Of The Issues Raised By The Cross-Petition Would Be Inappropriate Because The Court Of Appeals Did Not Pass Upon Them, And Because None Of The Reasons For Such Review Exists Here

1. It hardly needs emphasizing that, since the Court of Appeals expressly declined to consider and pass upon the issues raised by the cross-petition, and since the cross-petition therefore is simply seeking review of the District Court decision, such issues are not ripe for review by this Court and such review at this juncture would be premature and inappropriate. *Cf., e.g., Bivens* v. *Six Unknown Federal Narcotics Agents*, 403 U.S. 388, 397-398 (1971); *Owens* v. *Union Pacific Railroad Co.*, 319 U.S. 715, 724-725 (1943).

2. The Trustee argues that the refusal by the Court of Appeals to decide the issue of Bankruptcy Act jurisdiction "has left this action in a peculiar posture", because "if this Court were to accept certiorari [in No. 78-309] and reverse on the Section 17 question . . . the Trustee could find that he is out of federal court on his non-Section 17 [*i.e.*, common law] claims for relief without ever having had a resolution of the question of jurisdiction over those claims" (Cross-Petition, pp. 6-7). The Trustee's argument misses the point here and does not justify granting the cross-petition. It is obvious that if this Court were to reverse the decision of Court of Appeals majority on the "Section 17 question", this action could be remanded to the Court of Appeals and the Trustee could at that time assert *to the Court of Appeals* for resolution by it whatever arguments he has on the issue of jurisdiction over his common law claims.[8] In other words, and contrary to the Trustee's argument that "this action [is] in a peculiar posture", the Trustee is not likely to be foreclosed from asserting to the Court of Appeals such jurisdictional arguments as he is entitled to make.[9]

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[8]The Trustee also speculates that even if his federal Section 17(a) claim were to be left standing, the District Court could refuse to exercise pendent jurisdiction and put him "out of federal court" on his common law claims (Cross-Petition, p. 7). If that hypothetical situation actually were to arise, however, and should it be of any actual consequence to the Trustee, he then could raise the jurisdictional issue on appeal to the Court of Appeals from any judgment entered in this action.

[9]That the Trustee actually understands that the issues raised by the cross-petition are not ripe for review by this Court because they have not been passed upon by the Court of Appeals, and that his real interest is in not being foreclosed from raising those issues in the Court of Appeals should this Court reverse on the Section 17(a) issues, is seen from his assertion that "this Court should grant

3. Moreover, even if it be assumed that the Trustee were correct in speculating that upon reversal by this Court on the Section 17(a) issues he could be "out of federal court on his non-Section 17 [*i.e.*, common law] claims for relief without ever having had a [Court of Appeals] resolution of the question of jurisdiction over those claims", the Trustee will not in any event be foreclosed from litigating his common law claims. He simply will continue to proceed in his State Court Action, which is still pending and in which those very same claims are asserted. Thus, the worst consequence that could befall the Trustee as a result of the so-called "peculiar posture" of this action would be that he is relegated to the State Court Action to litigate his common law claims—hardly a matter of "national importance", to use the Trustee's words (Cross-Petition, p. 7), sufficient to warrant review by this Court. This is particularly so since that "worst consequence" is actually the proper result which should be achieved in this action—*i.e.*, the Trustee ought to litigate his common law claims in a common law forum (*i.e.*, in his State Court Action), and he ought not be permitted further to burden *both* the New York state courts (in the State

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certiorari at least for the purposes of remanding for orderly consideration of the jurisdictional issues by the Court of Appeals" (Cross-Petition, p. 7, see also p. 15). Of course, it is totally unnecessary to grant the cross-petition for that purpose, since the matter can be handled in any decision that would result from the granting of certiorari on Touche Ross' Petition in No. 78-309. *Cf.*, *e.g.*, *Marconi Wireless Co.* v. *Simon*, 246 U.S. 46, 57 (1918) (in reversing and remanding to the court of appeals, this Court declined to decide an issue not passed upon by the court of appeals because "to do this would call for the exercise on our part of a duty which it was the province of the court below to perform and *which doubtless it would have performed but for the error into which it fell . . . [The issues should] be considered for what they are worth by the court below, if duly presented and relied upon, when it comes hereafter to consider the controversy*" (emphasis added)).

Court Action) and the federal courts (in this action) with parallel but separate proceedings on those claims.[10]

4. There are other reasons why, although the Trustee hyperbolizes about "the national importance of the jurisdictional issue" (Cross-Petition, p. 7), that "issue" simply does not rise to any level of importance which could justify its review by this Court. For example, the decision of the District Court does not conflict, and the Trustee does not claim that it conflicts, with any controlling decision of this Court or with any such decision in any court of appeals.

5. Moreover, the District Court decision is based in substantial part on an essentially factual determination with which the Trustee disagrees—*viz.*, that there is no "consent" jurisdiction because the Trustee's common law claims "[do] not arise out of any work done for Weis by Touche [Ross] and for which Touche [Ross] filed a claim in the Weis liquidation", and because the claims therefore are "unrelated" (56a).[11] Such issues of fact are

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[10]A matter of "national importance" which does exist in this action, and which distinguishes Touche Ross' Petition in No. 78-309 from the Trustee's cross-petition, is the serious and substantial question of whether the Trustee and SIPC are to be permitted to "federalize"—*i.e.*, to create jurisdiction in the federal courts so as to compel them to accept the burden of deciding—what are nothing more than common law claims simply by alleging that the conduct complained of also violates Section 17(a) of the 1934 Act (see, *e.g.*, Petition in No. 78-309, p. 33). That question is squarely raised by Touche Ross' Petition, and is one so consequential for an already overburdened federal court system that this Court should grant Touche Ross' Petition to pass upon it.

[11]The Trustee asserts that the facts are different than as found by the District Court, and argues that "this case presents a uniquely appropriate *factual opportunity* for this Court to resolve the question" (emphasis added) (Cross-Petition, p. 12). The Trustee elsewhere asserts that the District Court "apparently believed [as does the Trustee] that mutuality under Section 68 should be the controlling standard" but simply "erred" in applying that standard to the facts (*Id.* at pp. 10-11 n.6).

simply not a proper subject for review on certiorari. *See, e.g., United States* v. *Johnston,* 268 U.S. 220, 227 (1925); *Southern Power Co.* v. *North Carolina Public Service Co.,* 263 U.S. 508, 509 (1924); *Houston Oil Co. of Texas* v. *Goodrich,* 245 U.S. 440 (1918).

6. At bottom, the District Court decision on the issues raised by the cross-petition is simply a lower court decision without substantial impact beyond the parties to this action and the specific factual situation presented. As such it does not warrant review by this Court, because it is "of importance merely to the litigants and [does] not present an issue of immediate public importance". *Rice* v. *Sioux City Memorial Park Cemetery, Inc.,* 349 U.S. 70, 79 n.2 (1955); *Layne & Bowler Corp.* v. *Western Well Works, Inc.,* 261 U.S. 387, 393 (1923). Although the Trustee asserts that the lower federal courts "have applied a number of different standards" with respect to determining the scope of "consent" jurisdiction (Cross-Petition, pp. 10-11), it is apparent—even if it be assumed that there is some actual conflict among the "different standards" (as opposed to mere variety in the language used by various courts to explain the same legal concept)—that here the District Court found jurisdiction to be lacking even under the most lenient of such "standards" (see also pp. 17-21, *infra*). The Trustee does talk at length of a general and purportedly "widely recognized" need to clarify jurisdictional issues which might arise under the Bankruptcy Act, and to "clarify for claimants and litigants in bankruptcy proceedings throughout the country their rights and liabilities in subjecting themselves to the jurisdiction of a Court of Bankruptcy" (*e.g.,* Cross-Petition, p. 9), but that generalized, abstract need—even assuming it to exist—does not justify the granting of certiorari here. *E.g., Rice* v. *Sioux City Memorial Park Cemetery, Inc., supra,* 349 U.S. at 74

("A federal question raised by a petitioner may be of 'substance' in the sense that, abstractly considered, it may present an intellectually interesting and solid problem. But this Court does not sit to satisfy a scholarly interest in such issues").

7. It also would be inappropriate to grant the cross-petition because, as shown hereinbelow, the District Court decision is clearly correct, and the Trustee's arguments to the contrary are clearly erroneous, if not frivolous.

8. Finally, resolution of the questions presented by the cross-petition would be of little prospective importance because of recent legislative developments. First, SIPA recently has been amended so as to delete certain references to Chapter X of the Bankruptcy Act which the Trustee misapprehends in order to support his jurisdictional contentions (see pp. 23-27 and nn. 17, 20-22, *infra*). Second, Congress has passed and sent to the President an act (H.R. 8200, 95th Cong., 2d Sess., 124 CONG. REC. H 11,047 (daily ed. Sept. 28, 1978), as amended) which would substantially reform the entire Bankruptcy Act and, more significantly, would completely change the jurisdictional provisions applicable to any future case similar to this one. *See* H.R. 8200, *supra*, Title II, Section 241, 124 CONG. REC. H 11,082 (daily ed. Sept. 28, 1978), *as amended by the Senate,* 124 CONG. REC. S 17,405 (daily ed. Oct. 6, 1978).

II

The District Court Correctly Held That Touche Ross Did Not "Consent" To Jurisdiction In This Plenary Action By Filing Proofs Of Claim

The District Court correctly held (56a-57a) that Touche Ross did not, by filing its proofs of claim in the Weis liquidation proceeding, "consent" to jurisdiction

with respect to the Trustee's common law claims in this plenary action, for at least two reasons. First, the filing of the proofs of claim calls into play only the *summary* jurisdiction of the bankruptcy court, and is insufficient to confer jurisdiction in this *plenary* action. Second, even if it were assumed that "consent" to jurisdiction in a *plenary* action could be inferred from filing a proof of claim to the same extent that consent to *summary* jurisdiction can be so inferred, there still would be no jurisdiction here because Touche Ross' proofs of claim would not have conferred jurisdiction of the Trustee's common law claims even in a summary proceeding.

A. The Proofs of Claim Do Not Confer Jurisdiction In This Plenary Action

Section 23 of the Bankurptcy Act, 11 U.S.C. § 46, limits a district court's subject matter jurisdiction over an action brought by a trustee, by providing that such jurisdiction exists only to the extent that, had the bankruptcy proceeding not been instituted, there would have been jurisdiction if the action were between the bankrupt and the defendant. From its first interpretation by this Court, and as the Trustee concedes (Cross-Petition, p. 7 n.5), Section 23 has been held to be a limitation on the jurisdiction of the district courts, and to reflect a Congressional intention to direct *plenary* actions by trustees to the State courts. *See, e.g., Bardes* v. *Hawarden Bank*, 178 U.S. 524, 538 (1900); *Kelley* v. *Gill*, 245 U.S. 116 (1917); *Schumacher* v. *Beeler*, 293 U.S. 367, 374 (1934); *Williams* v. *Austrian*, 331 U.S. 642, 649 (1947).

Section 23b also contains a provision which authorizes the exercise of federal jurisdiction "by consent of the defendant". The provision regarding consent was included as a concession to the defendant who "might

not object to—indeed would welcome—federal court jurisdiction." *Tenenbaum* v. *Walter E. Heller & Co.*, 308 F.Supp. 1085, 1087 and n.9 (S.D.N.Y. 1970) (citing remarks of Senator Lindsay at 30 Cong. Rec. 601-602 (1897)).

However, the filing of a proof of claim does not constitute such "consent" to *plenary* jurisdiction under Section 23. As the Tenth Circuit has unequivocally stated,

> "a claimant does not consent to the exercise of the bankruptcy court's plenary jurisdiction by filing his claim in the bankruptcy proceedings." *Katchen* v. *Landy*, 336 F.2d 535, 537 (10th Cir. 1964), *aff'd*, 382 U.S. 323 (1966).

Although in certain circumstances *summary* jurisdiction may be exercised on the basis of consent inferred from the act of filing a proof of claim, *plenary* jurisdiction may not be exercised on such a basis. *Tamasha Town & Country Club* v. *McAlester Const. Fin. Corp.*, 252 F.Supp. 80, 89 (S.D. Cal. 1966) ("the policy underlying the doctrine of consent to summary jurisdiction by acts of the claimant, is avoiding multiplicity of actions and permitting the casting of accounts between the parties. Neither of these would be advanced by extending the doctrine of consent by acts of the claimant to a plenary proceeding"). It is for reasons of judicial economy that courts have treated the act of filing a proof of claim as consent by the creditor to *summary* jurisdiction with respect to certain claims which a trustee wishes to assert as counterclaims in the liquidation proceeding itself (see pp. 17-18, *infra*). There is no justification (and the Trustee cites no authority) for permitting him—in derogation of the very reason for implying such consent in the first place—to utilize the doctrine of consent to

summary jurisdiction to assert his claims outside of the liquidation proceeding itself and in a separate *plenary* action.[12]

The type of consent which is necessary to support *plenary* jurisdiction under Section 23 is express consent by a defendant to the jurisdiction of the district court over the plenary action or consent by the defendant's pleading to the merits in the plenary action without objection to jurisdiction. 2 W. COLLIER, BANKRUPTCY ¶ 23.14, p. 602.[13] But where, as here, a defendant makes no answer on the merits and expressly objects to

[12]Moreover, it would have an obviously chilling effect upon the assertion of legitimate claims in bankruptcy proceedings to hold that the price to be paid by a claimant for filing a claim (no matter how relatively small and no matter if undisputed) is submission to *plenary* jurisdiction of any action to be commenced against that claimant by the trustee. The point is vividly demonstrated here, where Touche Ross filed claims in the liquidation proceeding aggregating only $79,636, and is therefore alleged to have "consented" to *plenary* jurisdiction over the trustee's claims in this action of $51,000,000.

[13]Courts have found consent to *plenary* jurisdiction in a general appearance and a plea on the merits, *Schumacher* v. *Beeler, supra*, 293 U.S. at 369 (declining to permit party, after these steps, to withdraw consent and contest jurisdiction); explicit admissions of jurisdiction and litigation on the merits, *Gins* v. *Mauser Plumbing Supply Co.*, 148 F.2d 974, 977 n.5 (2d Cir. 1945); a specific concession of jurisdiction and litigation on the merits, *Tilton* v. *Model Taxi Corp.*, 112 F.2d 86, 88 (2d Cir. 1940); litigation on the merits and a failure to object to jurisdiction, *Toledo Fence & Post Co.* v. *Lyons*, 290 Fed. 637, 639-640 (6th Cir. 1923); *In re Prima Co.*, 98 F.2d 952, 959 (7th Cir.), *cert. denied*, 305 U.S. 658 (1938); a stipulation that the court had jurisdiction, *Green* v. *Gage*, 186 F.2d 984, 986-987 (5th Cir. 1951); pleading to the merits and taking testimony, *Detroit Trust Co.* v. *Pontiac Savings Bank*, 196 Fed. 29, 31-32 (6th Cir. 1912), *aff'd*, 237 U.S. 186 (1915); answering on the merits or appearing in court to seek affirmative relief, *May* v. *Moss*, 194 F.2d 133, 137 (8th Cir.), *cert. denied*, 343 U.S. 952 (1952); and appearing, pleading to the merits, affirmatively requesting relief and litigating the merits at trial and on appeal, *Wymard* v. *McCloskey & Co.*, 342 F.2d 495, 497-498 (3d Cir.) (en banc), *cert. denied*, 382 U.S. 823 (1965) (3 judges dissented, taking the position that under the circumstances even these facts did not suffice to show consent to jurisdiction).

jurisdiction by moving to dismiss the action for lack of subject matter jurisdiction, no consent exists or may be implied under Section 23. *See Halpert* v. *Engine Air Service*, 116 F.Supp. 13, 15 (E.D.N.Y. 1953); *cf.*, *Stiefel* v. *14th Street & Broadway Realty Corp.*, 48 F.2d 1041, 1043 (2d Cir. 1931).

The Trustee's basic error in arguing for his so-called "consent" jurisdiction (Cross-Petition, pp. 7-12) lies in the fact that he simply ignores the clear distinction between this *plenary* action and whatever *summary* proceedings he might have commenced in the Weis liquidation proceeding by reason of Touche Ross' proofs of claim therein. Consequently, his entire argument is nothing more than a confusing hodgepodge of concepts purportedly applicable in *summary* proceedings, discussed on the patently erroneous assumption that those concepts automatically are applicable to separate *plenary* actions.

B. The Proofs Of Claim Would Not Confer Jurisdiction Even In A Summary Proceeding

It is also clear that the filing of Touche Ross' proofs of claim would not have conferred jurisdiction over the Trustee's common law claims even if he had asserted them as counterclaims in a *summary* proceeding. This is because, as the District Court expressly found, Touche Ross' claims and the Trustee's claims are "unrelated" (56a).

For reasons of judicial economy, courts have been willing to consider the act of filing a proof of claim as consent to summary jurisdiction of such counterclaims, where the claim and counterclaim are "related", "closely related" or "in the nature of 'compulsory counterclaims'" (see cases cited in Cross-Petition, pp.

11-12).[14] The Trustee concedes here that his common law claims (which arise from Touche Ross' mid-1972 audit of the 1972 Weis financial reports) and the Touche Ross claims in the Weis liquidation proceeding (which relate to services performed by Touche Ross in late 1972 and 1973) "may not be closely related enough to satisfy a strict compulsory counterclaim standard" (Cross-Petition, p. 12), although he does contend that there is some ill-defined, nebulous "logical relationship" between them *(id.)*—a contention expressly rejected by the District Court in finding that the claims are "unrelated". Dilution of the "relatedness" requirement recognized by the applicable cases to the extent which would be required to sustain "consent" jurisdiction of the Trustee's common law claims simply would make illusory the judicial economies which supposedly justify the doctrine of jurisdiction by implied consent.

The Trustee apparently recognizes the weakness of his contention that his claims satisfy some formulation of the "relatedness" requirement, because the main thrust of his argument is that such requirement should be abandoned, and that "consent" jurisdiction should ex-

[14]This prevents a trustee from having to present the same evidence twice, once before the bankruptcy judge to defend against a creditor's claim and once before the court with plenary jurisdiction to make his affirmative recovery. *See In re Farrell Publishing Co.*, 130 F.Supp. 449 (S.D.N.Y. 1955) ("The same proof will be required in defending against [the creditor's] claim as is necessary in the proof of the trustee's counterclaim"); *Columbia Foundry Co.* v. *Lochner,* 179 F.2d 630, 633 (4th Cir. 1950) (creditor must produce the same evidence to save his claim as he would to defeat an affirmative judgment against him on the counterclaim). Moreover, once a bankruptcy judge adjudicates the creditor's claim, principles of collateral estoppel would prevent relitigation of some if not all of the issues in a trustee's closely related counterclaim, so that requiring a trustee to bring a separate plenary action against the claimant to litigate a matter already settled between them would be to exalt form over substance. *Cf., Katchen* v. *Landy,* 382 U.S. 323, 333-335 (1966). *See also Giffin* v. *Vought,* 175 F.2d 186, 189-190 (2d Cir. 1949).

tend to *any* "mutual" claim capable of being set-off under Section 68a of the Bankruptcy Act, 11 U.S.C. § 108a. The Trustee relies upon *Katchen* v. *Landy,* 382 U.S. 323 (1966), which held only that by submitting a claim in bankruptcy a creditor subjects himself to the bankruptcy court's summary jurisdiction to order the return of a voidable preference and which concededly "did not decide whether the same rule applied to other types of claims by a Trustee" (Cross-Petition, p. 9), and upon *dictum* in a Second Circuit decision, *Conway* v. *Union Bank of Switzerland,* 204 F.2d 603, 607 (2d Cir. 1953). However, the Trustee acknowledges that "the lower federal courts have not applied the same rationale as *Katchen*", and that the *dictum* in *Conway* is inconsistent with subsequent holdings in the Second Circuit itself (Cross-Petition, pp. 10-11).

There are good reasons for not extending the *Katchen* rationale to any unrelated "mutual" claim capable of being set-off under Section 68a. In the first place, "[i]t should be remembered that [Section] 68 constitutes merely a statutory recognition of an accepted doctrine, with exceptions thereto, and does not govern the question of jurisdiction of a court to give effect to the doctrine". 4 W. COLLIER, BANKRUPTCY ¶ 68.02[1] at 854. Moreover, although (as the Trustee points out—Cross-Petition, p. 9) in the *Katchen* situation "the determination of whether a claimant has received a voidable preference [was] a prerequisite to determining the size and allowability of his claim under Section 57g of the Bankruptcy Act", determination of "mutual" claims pursuant to Section 68a is not (as the Trustee incorrectly argues, *id.* at p. 10) such a prerequisite, because the provisions of Section 68a have been held to be "permissive rather than mandatory". *Cumberland Glass Manufacturing Co.* v. *De Witt & Co.,* 237 U.S. 447, 455 (1915).

The *Katchen* holding was premised expressly upon the need to make the bankruptcy laws " 'inexpensive in [their] administration' " and " 'to secure a prompt and effectual administration and settlement of the estate of all bankrupts within a limited period' ". 382 U.S. at 328. However, to extend the *Katchen* rationale to any unrelated mutual claim would conflict with *Daniel* v. *Guaranty Trust Co.*, 285 U.S. 154 (1932), in which this Court rejected the contention that a creditor by filing a claim for reclamation of property "entered its general appearance and in effect consented to submit itself to summary proceedings . . . in respect of matters having no immediate relation to the claim which it had presented". *Id.* at 162. In *Daniel* this Court found administrative needs not to be sufficiently compelling so as to require a creditor, as the price for filing a claim, to relinquish the procedural safeguards which would be available in a plenary action brought by the Trustee on his unrelated claims:

> "In practice such a rule might lead to unfortunate complications and deprive owners of property of fair opportunity to recover. The risk incident to a general appearance and consent to adjudication of claims of all kinds might easily deter where the right to recover is clear. Moreover, the choice would not be between tribunals merely, but between the ordinary processes in a plenary suit and a summary hearing. . . . We cannot conclude that the demand for speedy administration of bankrupt estates is enough to justify such a radical departure from ordinary procedure." 285 U.S. at 162.[15]

[15]The summary jurisdiction of the bankruptcy judge abrogates a claimant's right to trial by jury which he would have if he had not filed his claim but rather abided the trustee's plenary suit, *Katchen* v. *Landy*, *supra*, 382 U.S. at 336-340 (1966), a right normally entitled to great deference, *Beacon Theatres* v. *Westover*, 359 U.S. 500, 510-511 (1959) (right to jury trial lost "only under the most imperative circumstances"). Consequently, courts have been very cautious in enlarging that summary jurisdiction. *See In re Behring & Behring*, 445 F.2d 1096, 1098-1099 (5th Cir.), *cert. denied*, 404 U.S. 991 (1971); *Gill* v. *Phillips*, 337 F.2d 258, 262-263 (5th Cir. 1964); *In re Carnell Constr. Corp.*, 424 F.2d 296, 298 (3d Cir.), *cert. denied*, 400 U.S. 828 (1970); *In re Beasley-Gilbert's, Inc.*, 285 F.Supp. 359, 363 (S.D. Ohio 1968); Ferguson, *The Consensual Basis of Subject-Matter Jurisdiction in Matters of Bankruptcy: Fact and Fiction*, 14 Rutgers L. Rev. 491, 493, 511 (1959).

Moreover, the Trustee cannot retain the jurisdictional basis recognized in *Katchen* and at the same time cure the obvious injustice to the creditor recognized in *Daniel* simply by commencing (as was done here) a separate federal plenary action. Although such a plenary action would eliminate the procedural disadvantages to the creditor of a summary proceeding, it also would eliminate the reasons of judicial economy upon which the *Katchen* rationale is premised (see also pp. 17-18, *supra*). The *Katchen* holding thus simply cannot be extended, consistent with the concerns recognized in *Daniel* and other cases (see p. 18 n.14, *supra*), to any unrelated "mutual" claim asserted by the Trustee.

III

The District Court Correctly Held That Section 23 Of The Bankruptcy Act Is Applicable To Preclude The Exercise Of Bankruptcy Act Jurisdiction, And That The Other Statutory Provisions Relied Upon By The Trustee Do Not Require A Contrary Result

The District Court correctly held (55a-56a) that this action "is controlled by [Section 23 of the Bankruptcy Act] 11 U.S.C. § 46 which [is incorporated into SIPA by Section 6(c)(1) thereof and which] provides that a trustee in bankruptcy may sue only in the courts where

the bankrupt might have sued", and that subject matter jurisdiction of the Trustee's common law claims is lacking because "[d]iversity jurisdiction would not exist of an action by Weis against Touche [Ross]". The Trustee erroneously argues that the District Court was incorrect (Cross-Petition, p. 14), and that under other statutory provisions—*viz.*, Sections 5(b)(2) and 6(b)(1) of SIPA and Section 115 of the Bankruptcy Act—the District Court had "the 'powers' of a Chapter X court and a federal equity receivership court" and thus had "*plenary* jurisdiction over any action commenced by the Trustee" (*id.* at pp. 4, 13-14).

A. Section 23 Is Incorporated Into SIPA By Section 6(c)(1) Thereof And Applies Here To Preclude Bankruptcy Act Jurisdiction

Section 6(c)(1) of SIPA makes applicable to all SIPA liquidations "the provisions of Chapter X and such of the provisions . . . of Chapters I to VII, inclusive, of the Bankruptcy Act as section 102 of Chapter X would make applicable if an order of the court had been entered directing that bankruptcy be proceeded with pursuant to the provisions of such Chapters I to VII". Section 102 of the Bankruptcy Act, which is part of Chapter X, expressly provides that Section 23 will apply when an order of the type referred to in Section 6(c)(1) of SIPA (*i.e.*, an order "directing that bankruptcy be proceeded with") is entered.[16]

Thus, as the District Court properly recognized, the combination of Section 6(c)(1) of SIPA and Section 102 of the Bankruptcy Act results in Section 23 of the Bankruptcy Act being applicable in all SIPA liquidation

[16]Section 6(c)(1) of SIPA and Section 102 of the Bankruptcy Act are more fully set forth in the appendix to the cross-petition.

proceedings. *See Securities and Exchange Commission* v. *Morgan Kennedy & Co., Inc.*, [1973-1974 Transfer Binder] FED. SEC. L. REP. (CCH) ¶94,568 at p. 95,966 (S.D.N.Y. 1974); 6 W. COLLIER, BANKRUPTCY ¶1.06 at 209. That result is entirely consistent with the Congressional recognition in Section 6(a)(4) of SIPA that the overriding purpose of a SIPA proceeding is "to liquidate the business of the debtor" and the reiteration in Section 6(c)(1) that "in no event shall a plan of reorganization be formulated". *Cf.* 6 W. COLLIER, BANKRUPTCY ¶3.18 at 547-548 (reasons for suspension in Chapter X *reorganizations* of limitations imposed by Section 23 are inapposite when bankruptcy liquidation is to be proceeded with).[17]

Since Section 23 permits the Trustee to assert his common law claims here only if there would have been diversity jurisdiction in an action by Weis against Touche Ross (see p. 6, *supra*), and since no such diversity jurisdiction would have existed (see p. 6 n. 6, *supra*), Section 23 operates here—as the District Court held—to deprive it of jurisdiction over the Trustee's common law claims.

[17]Recently, and more than two years after this action was commenced, SIPA was amended by Pub. L. No. 95-283, 92 Stat. 249 (May 21, 1978). The reference to Section 6(c)(1) is to that section as in effect prior to such amendment. As amended, the section (now renumbered Section 6(b), 15 U.S.C.A. § 78fff(b) (Supp. II 1978)) provides that "a liquidation proceeding shall be conducted in accordance with, and as though it were being conducted under, the Bankruptcy Act". Pursuant to amended Section 16(1), 15 U.S.C.A. §78lll(1) (Supp. II 1978), "[t]he term 'Bankruptcy Act' means . . . those provisions of the Bankruptcy Act relating to ordinary bankruptcy (chapters I through VII)". The purpose of the amendment was to "eliminate the wholesale incorporation of chapter X of the Bankruptcy Act". S. REP. No. 95-763, 95th Cong. 2d Sess., *reprinted in* [1978] U.S. CODE CONG. & AD. NEWS 1344, 1354. Under the amended statute, as under the statute prior to amendment, Section 23 is applicable and the plenary jurisdiction of the district court is limited as in ordinary bankruptcy under Chapters I through VII. The amendment simply makes more clear that the Chapter X reorganization provisions relied upon by the Trustee are inapplicable.

B. Sections 5(b)(2) And 6(b)(1) Of SIPA Do Not Provide Jurisdiction For The Trustee's Common Law Claims

The Trustee erroneously argues that Sections 5(b)(2) and 6(b)(1) of SIPA confer on the District Court jurisdiction of his common law claims (Cross-Petition, pp. 13-14).

1. SECTION 5(b)(2).—The Trustee erroneously asserts that jurisdiction of his common law claims is provided by the language—which he takes out of context—of Section 5(b)(2) that the court in a SIPA proceeding shall have the "*powers* . . . of a court of bankruptcy and of a court in a proceeding under Chapter X of the Bankruptcy Act" (Cross-Petition, p. 13). The full sentence of Section 5(b)(2) from which the Trustee selectively quotes reads as follows (with the critical portion omitted by the Trustee set forth in italics):

> "Upon the filing of an application pursuant to subsection (a)(2) of this section, the court to which application is made shall have *exclusive jurisdiction of the debtor involved and its property wherever located* with the powers, to the extent consistent with the purposes of this act, of a court of bankruptcy and of a court in a proceeding under chapter X of the Bankruptcy Act" (emphasis added).

The italicized words make clear that this sentence of Section 5(b)(2) applies only to the *summary* jurisdiction of the bankruptcy judge over the debtor and his assets, and is not a section providing plenary jurisdiction over actions against third persons. Although the legislative history does not discuss the sentence, its language is

familiar from the Bankruptcy Act [18] and has uniformly been held therein to provide for summary jurisdiction of a bankruptcy judge over the assets in the possession of the debtor, essentially a form of *in rem* jurisdiction.[19] Of course, it is well-settled by this Court that claims against third persons may not be adjudicated under the summary jurisdiction of the bankruptcy courts, but must be the subject of a plenary suit, *e.g.*, *Cline* v. *Kaplan*, 323 U.S. 97 (1944); *Taubel-Scott-Kitzmiller* v. *Fox*, 264 U.S. 426 (1924); *Kelley* v. *Gill*, 245 U.S. 116 (1917); *Harrison* v. *Chamberlin*, 271 U.S. 191, 193-195 (1926), and the cases recognize that the summary jurisdiction conferred by the "exclusive jurisdiction" language of the Bankruptcy Act sections referred to above does not extend to a power to adjudicate claims against third persons. Moreover, the context in which the "powers" language of Section 5(b)(2), upon which the Trustee relies, is used demonstrates that it means "powers" with respect to the property over which the court has jurisdiction—*i.e.*, the

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[18] Such language is used in Section 75(n), 11 U.S.C. § 203(n) (farmer's relief); Section 77, 11 U.S.C. § 205 (railroad reorganizations); Section 77B(a), Act of June 7, 1934, § 77B(a), 48 Stat. 911, 912 (predecessor of Chapter X; now repealed); Section 82(a) of Chapter IX, 11 U.S.C. § 402(a); Section 111 of Chapter X, 11 U.S.C. § 511; Section 311 of Chapter XI, 11 U.S.C. § 711; Section 411 of Chapter XII, 11 U.S.C. § 811; and Section 611 of Chapter XIII, 11 U.S.C. § 1011.

[19] *E.g.*, *In re Standard Gas & Elec. Co.*, 119 F.2d 658, 661, 662 (3d Cir. 1941) (Section 77B(a)). *See also, e.g.*, *Continental Illinois Nat'l Bank & Trust* v. *Chicago, R.I. & Pac. Ry. Co.*, 294 U.S. 648, 681-684 (1935) (Section 77); *In re Prudence Bonds Corp.*, 75 F.2d 262 (2d Cir. 1935) (Section 77B(a)); *Thompson* v. *Terminal Shares*, 104 F.2d 1, 9 (8th Cir. 1939) (Section 77B(a)); *Mar-Tex Realization Corp.* v. *Wolfson*, 145 F.2d 360, 362-363 (2d Cir. 1944) (Section 111); *Duda* v. *Sterling Mfg. Co.*, 178 F.2d 428 (8th Cir. 1949) (Section 111); *Slenderella Systems of Berkeley, Inc.* v. *Pacific Tel. & Tel.*, 286 F.2d 488 (2d Cir. 1961) (Section 311); *In re Oliver*, 127 F.Supp. 842, 845-847 (D. Kan. 1955) (Section 611); *Tamasha Town & Country Club* v. *McAlester Constr. Fin. Corp.*, 252 F.Supp. 80, 85 and n.1 (S.D. Cal. 1966) (Section 311).

power to use all the remedial devices a bankruptcy court or a Chapter X court might use to protect the debtor's property.

Since Section 5(b)(2) uses precisely the same language as is found in the Bankruptcy Act, and since that language has been expressly held not to confer plenary jurisdiction over actions brought by a trustee against third persons, Section 5(b)(2) cannot properly be read to provide such jurisdiction over the Trustee's common law claims. *See Securities & Exchange Commission* v. *Morgan Kennedy & Co., supra,* [1973-1974 Transfer Binder] FED. SEC. L. REP. (CCH) ¶94,568 at p. 95,971.[20]

2. SECTION 6(b)(1).—The Trustee errs in suggesting that Section 6(b)(1) of SIPA has some relevance to determining the District Court's jurisdiction (Cross-Petition, p. 13). Section 6(b)(1) prescribes only the powers of a SIPA trustee, and has nothing to do with the jurisdiction of a district court.[21]

C. Section 115 Of The Bankruptcy Act Does Not Provide Jurisdiction For The Trustee's Common Law Claims

The Trustee's assertion that Section 115 of Chapter X is a grant of jurisdiction is erroneous. Section 115 confers upon a Chapter X court only the "powers" of an equity receivership court, whereas in the same sentence it also speaks of the "jurisdiction, powers and duties" otherwise conferred. This clearly shows that Congress understood that the terms "powers" and "jurisdiction" in Section 115 signified separate and distinct concepts

[20]Section 5(b)(2), as amended in 1978, 15 U.S.C.A. §78eee(b)(2) (Supp. II 1978), even deletes the "powers . . . of a court in a proceeding under Chapter X" language relied upon by the Trustee.

[21]As amended in 1978, that section (which is renumbered Section 7(a), 15 U.S.C.A. §78fff-1(a) (Supp. II 1978)) also deletes the reference to the "powers" of a Chapter X trustee upon which the Trustee relies.

and compels the conclusion that Congress intended to confer only "powers" and not "jurisdiction". *See* 6 W. COLLIER, BANKRUPTCY ¶3.18 at 546-547 n. 34.[22]

Congress took the language of Section 115 from the virtually identical language of Section 77B(a) of the Bankruptcy Act, which had been enacted in the Corporate Reorganization Act of 1934.[23] It was uniformly held that Section 77B(a) did not create a grant of jurisdiction to the district courts. *In re Prudence Bonds Corp., supra,* 75 F.2d at 263; *United States* v. *Tacoma Oriental S. S. Co.,* 86 F.2d 363, 368 (9th Cir. 1936); *In re Standard Gas & Elec. Co., supra.*

A consistent series of cases has interpreted the "powers" language of Section 115 and the predecessor language of Section 77B to mean the non-jurisdictional substantive powers over property exercised by a court of equity. As the Third Circuit phrased it, with regard to Section 77B(a),

> "This reference to the powers which a federal equity court exercises when it appoints a receiver is to the substantive powers which such a court exercises over the property in its custody rather than to its jurisdiction to entertain plenary suits growing out of the receivership." *In re Standard Gas & Elec. Co., supra,* 119 F.2d at 662.

Accord, In re Prudence Co., 82 F.2d 755, 757 (2d Cir.), *cert. denied,* 298 U.S. 685 (1936); *In re Prima Co.,* 98 F.2d 952, 958 (7th Cir.), *cert. denied,* 305 U.S. 658 (1938).

[22]The 1978 amendments to SIPA deleting wholesale incorporation of Chapter X provisions eliminate any incorporation into SIPA of the provisions of Section 115.

[23]In enacting Chapter X, "[b]y and large . . . the substance of section 77B is preserved" and "[s]ection 115 is derived from section 77B(a), with only minor changes in language." S. REP. No. 1916, 75th Cong., 3d Sess. at 19, 24 (1938). Hence, decisions interpreting Section 77B(a) are applicable to Section 115.

Williams v. *Austrian, supra,* relied upon by the Trustee, actually found it unnecessary to reach the issue of whether Section 115 was jurisdictional because of its holding that, in light of Section 102's suspension of the limitations of Section 23 during reorganization, jurisdiction there existed by virtue of Section 2a(7). In the footnote referred to by the Trustee, this Court, after pointing out the decisions which held the "powers" language of Section 77B and Section 115 to be "non-jurisdictional", merely cited *dicta* in two other lower court cases as conflicting interpretations. *Id.* at 659-600 n. 45.[24]

Finally, even if the "powers" language of Section 115 were assumed to be a grant of jurisdiction, Section 23 would limit that jurisdiction. The "powers" provided for in Section 115 are those "not inconsistent with the provisions of this chapter". One of the provisions of "this chapter" is Section 102, which explicitly makes Section 23 applicable in the liquidation context present here.[25] *Cf., e.g., In re Standard Gas & Electric Co., supra,* 119 F.2d at 660-663 (Section 23 incorporated into

[24]The Trustee also erroneously relies on the holding of *Williams* v. *Austrian* that broad plenary jurisdiction under Section 2a(7) of the Bankruptcy Act, unlimited by the restrictions set forth in Section 23 thereof, exists in a Chapter X reorganization. As *Williams* v. *Austrian* makes clear, such jurisdiction is available only by virtue of Section 102's suspension of Section 23 *while reorganization actually is proceeding.* Section 6(c)(1) of SIPA provides, however, that Section 102 must be read as if bankruptcy liquidation has been ordered, under which circumstance Section 102 requires termination of any suspension of Section 23.

[25]The similar phrase in Section 2a(7), "except as herein otherwise provided", has been consistently held to be a reference to Section 23. *Williams* v. *Austrian, supra,* 331 U.S. at 649; *First National Bank* v. *Title & Trust Co.,* 198 U.S. 280, 298 (1905); *Bryan* v. *Bernheimer,* 181 U.S. 188, 194 (1901); *Bardes* v. *Hawarden Bank, supra,* 178 U.S. at 535-536.

Section 77B); *Tilton* v. *Model Taxi Corp.,* 112 F.2d 86, 88 (2d Cir. 1940) (Section 23 held to control jurisdiction under Section 77B, despite the presence there of the predecessor language to Section 115); *In re Prima Co., supra,* 98 F.2d at 958 (the predecessor language to Section 115 did not "amount to a repeal by implication of Section 23").

CONCLUSION

For the foregoing reasons, the Trustee's cross-petition for a writ of certiorari should be denied.

October 23, 1978

Respectfully submitted,

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